

**Text of Proposed Amendments to
California Code of Regulations, Title 18, Section 1618**

Section 1618. United States Government Supply Contracts.

(a) Definitions.

(1) "United States Government supply contract" means a contract with the United States to furnish, or to fabricate and furnish, tangible personal property including ships, aircraft, ordnance, or equipment, whereby title to tangible personal property purchased for use in fulfilling the contract passes to the United States pursuant to the title provisions contained in the contract before the contractor uses the property to perform the function or act for which the property was designed or manufactured. The term "U.S. Government supply contract" does not include contracts to construct improvements on or to real property or to the purchase of tangible personal property for use in fulfilling such contracts.

(2) "Direct consumable supplies" means supplies, tools, or equipment consumed in the performance of a contract which are specifically identified to the contract and the actual cost of which is charged as a direct item of cost to the specific contract. ~~"Tools" as used in this definition does not include "special tooling" subject to the provisions of Federal Acquisition Regulation (FAR) 52.245-17 or any regulation(s) which succeeds FAR 52.245-17.~~ Effective June 14, 2007, "Tools" as used in this definition includes "special tooling" that was previously covered by Federal Acquisition Regulation (FAR) 52.245-17.

(3) "Overhead materials" means supplies consumed in the performance of a contract the cost of which is charged to an overhead expense account and then allocated to various contracts based on generally accepted accounting principles and consistent with government cost accounting standards.

(b) Application of Tax.

(1) Sales to U.S. Government supply contractors of tools, equipment, direct consumable supplies and overhead materials are sales for resale if the United States takes title pursuant to a United States government supply contract prior to any use of the property by the contractor to perform the function or act for which the property was designed or manufactured. Accordingly, tax does not apply to such sales even though the property does not become a component part of the tangible personal property furnished, fabricated, or manufactured by the contractor. If the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the passage of title to the United States, tax applies to the sales to or to the use by the contractor.

(2) Whether title to direct consumable supplies ~~and~~ or indirect consumable supplies (i.e., overhead materials) passes to the United States under a United States government supply contract and the time at which title passes will be determined in

accordance with the title provisions contained in the contract, if any. ~~In a case where the cost of~~

(A) For direct consumable supplies, which are charged direct to the United States government contract, title passes to the United States government pursuant to the title passage clause(s) associated with that specific contract.

(B) For indirect consumable supplies (i.e., overhead materials), which are charged to an expense account which is then allocated to various locations, cost centers or contracts, ~~some of which are engaged in other than United States government cost reimbursement contracts and/or fixed price contracts with a progress payments clause,~~ it will be considered that title ~~did not pass~~ to the United States government prior to use of the property, and tax will not apply with respect to the purchase or use of the property charged to the expense account, ~~unless~~ if the item is ~~specifically accounted for as being charged~~ allocated to a specific United States government supply contract, pursuant to the terms of which title passes to the United States prior to the use of the item. Property will be considered ~~charged~~ allocated to a specific United States government supply contract when it is allocated pursuant to:

~~(1) a1.~~ Accounting standards promulgated by the Cost Accounting Standards Board (Office of Federal Procurement Policy, Office of Management and Budget), if applicable; otherwise,

~~(2) g2.~~ Generally accepted accounting principles that are equitable, consistently-applied, and appropriate to the particular circumstances.

Direct consumable supplies identified in subdivision (b)(2)(A) and indirect consumable supplies (i.e., overhead materials) which may be allocated in ~~this~~ the manner identified in subdivision (b)(2)(B) include, but are not limited to, property used to repair items of capital equipment when a portion of the contractor's use is properly allocable to its government supply contracts, notwithstanding the fact that title to the property being repaired remains with the contractor.

(3) Special Tooling. Effective December 29, 1989 through June 13, 2007, title will generally not pass prior to use by the contractor for special tooling which is subject to the Special Tooling Clauses of Federal Acquisition Regulation (48 CFR) 52.245-17. Title to such special tooling will pass prior to use by the contractor only if the agreement between the contractor and the United States government contains a custom clause providing for title passage prior to use by the contractor. Therefore, sales of special tooling will generally be subject to tax.

Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Sections 6007 and 6381, Revenue and Taxation Code; and Aerospace Corp. v. St. Bd. of Equalization (1990) 218 Cal.App.3d 1300.